



11 November 2011

Ms Christine Barron
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The Treasury
Langton Crescent
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By email: cgt_natural_disasters@treasury.gov.au

Dear Christine

Proposals Paper – Capital gains tax relief for taxpayers affected by natural disasters

The Institute of Chartered Accountants in Australia (the **Institute**) welcomes the measures outlined in the Proposals Paper which are intended to provide capital gains tax (**CGT**) relief to taxpayers affected by natural disasters where they participate in:

- an Australian government agency assistance program that provides replacement assets to taxpayers affected by natural disasters, or
- cash grant programs operated by a government agency or another entity.

Our comments on the options in the Proposals Paper are set out below.

Government agency replacement asset programs

The changes put forward seek to overcome the following issues which arise where, under a government agency replacement asset program, a qualifying taxpayer swaps an existing post-CGT asset (**original asset**) for a replacement asset in circumstances where rollover may or may not apply.

Where rollover does not apply, the proposed amendments seek to address the following issues:

- the triggering of a capital gain or loss, being the difference between the market value of the replacement asset and the cost base (or reduced cost base) of the original asset (with no cash sale proceeds to fund the tax liability on any capital gain)
- the fact that the cost base of the replacement asset is the market value of the original asset which is likely to be depressed as a result of the natural disaster
- the difficulty of establishing the cost base of the original asset where records have been destroyed and the cost base cannot be reconstructed
- the requirement to obtain valuations of both the original and replacement asset.

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Even where existing rollover relief is available, determining the cost base of the original asset which becomes the cost base of the replacement asset may be difficult if records have been destroyed.

To address or alleviate these issues it is proposed that taxpayers participating in such programs be able to choose a CGT exemption with the result that:

- any capital gain or loss which would otherwise arise is disregarded, and
- the cost base of any replacement asset is its market value (and not the market value of the original asset).

The proposed amendments obviate the need for taxpayers to determine the cost base of the original asset which we believe is an appropriate outcome in the circumstances contemplated.

However, where taxpayers are willing and able to establish the cost base of their original asset we recommend that the CGT exemption allow them to choose that the cost base or reduced cost base of their replacement asset be:

- the market value of the replacement asset, or
- the cost base of their original asset.

This would be more equitable to taxpayers in circumstances where the cost base of the original asset is higher than the market value of the replacement asset. For example, assume:

	\$
Cost base of original land	150,000
Market value of original land following the natural disaster	50,000
Market value of replacement land	130,000

The consequences of entering into a land swap arrangement are as follows:

	Existing law	Proposed law
	\$	\$
Capital gain(loss)	(20,000)	Disregard
Cost base of replacement asset	50,000	130,000

By choosing the CGT exemption as proposed, the taxpayer can access a cost base of the replacement land of \$130,000 but forgoes the \$20,000 capital loss in order to do so.

In our view, a more equitable outcome would be to allow the taxpayer to choose a cost base of the replacement land of \$150,000, being the cost base of the original land.

Proposed application dates for rights under assistance programs

Chapter 3 highlights that taxpayers participating in an Australian government agency replacement asset program may receive rights under that program which are CGT assets. Similarly, taxpayers affected by a natural disaster that apply for a cash grant from a government agency or another entity may also receive rights under that cash grant program which are CGT assets. As a consequence, when a CGT event happens to such rights, e.g. extinguishment of the right when a cash payment is received, taxpayers may realise a capital gain or loss.

It is proposed that, where a CGT event happens after 1 July 2011 in respect of such rights, any capital gains or losses which a taxpayer may realise would be disregarded.



We understand that any rights to participate in an Australian government agency replacement asset program will have arisen after 1 July 2011. So, targeting the proposed changes to CGT events which occur after 1 July 2011 in respect of rights under these programs appears appropriate.

However, we are advised that taxpayers in Queensland received rights under certain government and community organisation cash grant programs before 1 July 2011. In these circumstances we suggest that the rationale for the 1 July 2011 date be explained in the Explanatory Memorandum to allay any concerns that taxpayers adversely affected by the same natural disaster are being treated differently. If in fact such taxpayers are being treated differently, the 1 July 2011 date should be reconsidered on policy grounds.

More broadly, the Explanatory Memorandum should explain the interaction between the proposed CGT relief measures and the amendments made by *Tax Laws Amendment (2011 Measure No 1) Act 2011*. In broad terms, based on the Explanatory Memorandum to that Act, we understand that the effect of the amendments is to treat as non-assessable non-exempt income certain government disaster relief payments claimed by small businesses and primary producers between 9 January and 1 March 2011 that relate to flooding that occurred in Australia after 28 November 2010 or the impact of Cyclone Yasi.

In summary, our view it is important that all taxpayers adversely affected by the same event(s) be treated equally and that it be apparent from comments in the Explanatory Memorandum that this is the case.

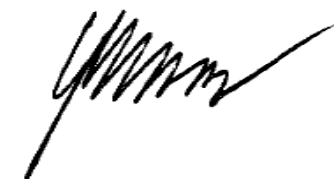
Other issues

We are aware that at least one other submission to Treasury in relation to the Proposals Paper raises the issue of the operation of the cost base apportionment rules in section 112-30 of the ITAA 1997 where a composite asset is partly destroyed, e.g. the buildings on post-CGT land, where there are no capital proceeds for the destruction of part of the asset.

In our view, consideration should be given to whether that rule interacts appropriately with the CGT exemption proposed in the Paper.

Should you have any questions in relation to our submission please call Susan Cantamessa on 02 9290 5625.

Yours sincerely



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The Institute of Chartered Accountants in Australia

